

## **Finding 1. Apparent Corporate Contributions**

### **Summary**

During the campaign, the Candidate made 11 loans to RRFC totaling \$585,090 which appeared to have originated from corporate accounts. In response to the interim audit report, RRFC maintained that all loans from the Candidate were made utilizing personal funds. RRFC submitted various documents in support of its position. Based on the documentation submitted, it appears that loans of \$369,090 were made using impermissible corporate funds.

### **Legal Standard**

**A. Corporate Contributions Impermissible.** A corporation is prohibited from making any contribution in connection with a federal election. 2 U.S.C. §441b(a).

**B. Receipt of Prohibited Contributions – General Prohibition.** Candidates and committees may not accept contributions (in the form of money, in-kind contributions or loans):

1. In the name of another; or
2. From the treasury funds of the following prohibited sources:
  - Corporations (this means any incorporated organization, including a non-stock corporation, an incorporated membership organization, and an incorporated cooperative);
  - Labor Organizations;
  - National Banks;
  - Federal Government Contractors (including partnerships, individuals, and sole proprietors who have contracts with the federal government); and
  - Foreign Nationals (including individuals who are not U.S. citizens and not lawfully admitted for permanent residence; foreign governments and foreign political parties; and groups organized under the laws of a foreign country or groups whose principal place of business is in a foreign country, as defined in 22 U.S.C. §611(b)). 2 U.S.C. §§441b, 441c, 441e, and 441f.

**C. Definition of Personal Funds.** Personal funds include salary and other earned income from bona fide employment and dividends and proceeds from the sale of the candidate's stock or other investments. 11 CFR §110.10(b)(2).

### **Facts and Analysis**

The Audit staff reviewed \$763,090 in loans reported by RRFC as made by the Candidate. The Candidate loaned RRFC \$404,090 during December of 2001, and the remaining \$359,000 was loaned throughout 2002.

The Audit staff reviewed the source of funds for all the Candidate loans and determined that \$585,090<sup>1</sup> appeared to have been funded with monies from the following corporations:

<sup>1</sup> Two additional loans (\$178,000) arose when RRFC made repayments to the Candidate for some of the corporate loans during October, 2002. The Candidate deposited those funds into his personal bank account and then loaned

- Renzi & Co., Inc.<sup>2</sup>, a subchapter S corporation<sup>3</sup> in which the Candidate held a 90% interest; and
- Fountain Realty and Development, Inc. (formerly Renzi Investments, Inc.<sup>4</sup>), a subchapter S corporation in which the Candidate held a 50% controlling interest.

During the audit fieldwork, the Audit staff reviewed selected bank statements, canceled checks, and other documents provided by RRFC, the Candidate, and the corporations. In addition, portions of the 2001 tax returns for the Candidate and the corporations<sup>5</sup> were reviewed. Our analysis of the documents available when the interim audit report was prepared indicated:

- The loans were made by check drawn on the corporate accounts, deposited into the Candidate's personal bank account, and then transferred by wire or check to RRFC's bank account.
- None of the checks drawn by the corporations to the Candidate indicated they were distributions of income to the Candidate.
- The Candidate's tax returns disclosed both salary and profit distributions from these corporations. The salary reported by the Candidate was not the source of the loans to the campaign. The profit distributions represent the Candidate's share of business profits for the year<sup>6</sup> and do not necessarily correspond to payments to the Candidate. The sum of the profits reported on the Candidate's tax return for 2001 is only about 20% of the amount loaned in that year. In addition, documentation was not provided to establish how, if at all, the amounts paid to the Candidate and subsequently loaned to RRFC relate to profit distributions.
- Although RRFC representatives indicated that the sale of 50% of the Candidate's interest in Fountain Realty & Development, Inc. was a source of funds for some

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those funds back to RRFC. Since the original source of the loans was the corporations, adding these loans to the total would constitute a double count. Therefore, these loans (\$178,000) are not considered.

<sup>2</sup> Renzi & Co., Inc. is now known as Patriot Insurance Agency, Inc.

<sup>3</sup> A subchapter S corporation (also called S corporation) is a general corporation that has elected a special tax status with the IRS. Subchapter S corporations are most appropriate for small business owners and entrepreneurs who prefer to be taxed as if they were still sole proprietors or partners. Subchapter S corporations avoid "double taxation" (once at the corporate level and again at the personal level) because all income or loss is reported only once on the personal tax returns of the stockholders. Subchapter S corporations are separate legal entities from its stockholders.

<sup>4</sup> Renzi Investments, Inc., was a subchapter S corporation wholly owned by the Candidate. When the Candidate sold a 50% interest in this entity, the name became Fountain Realty & Development, Inc.; which is how the Audit staff will refer to it in this report.

<sup>5</sup> Corporate tax returns were provided for Renzi & Co., Inc. (now Patriot Insurance Agency, Inc.), Renzi Investments, Inc. (now Fountain Realty & Development, Inc.), and Fountain Hills Estates Realty & Construction, Inc. (now Renzi Vino, Inc.). However, documentation was not presented to link Fountain Hills Estates Realty & Construction, Inc. to any of the Candidate loans.

<sup>6</sup> In the case of Fountain Hills Estates Realty & Construction, Inc. (not Fountain Realty & Development, Inc.) the tax return reflects a small loss.

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of the loans<sup>7</sup>, the documentation available at that time did not support that representation. According to the Candidate's tax return for 2001, the sale took place August 24, 2001; however, the loans were made in December 2001, more than three months after the sale. Bank records for the Candidate, Renzi & Co., Inc. and Fountain Realty & Development, Inc. were provided only for December 2001, and did not establish how and when the proceeds of the sale were received by the Candidate. Other documents detailed the sale of the interest to two individuals; however, no information concerning how the purchase price was determined was provided.

At the exit conference, the Audit staff presented this matter to RRFC representatives. They maintained that the funds in question were generated through the sale of various business assets. They argued that these business entities were owned solely or in majority by the Candidate; therefore, profits from the sale of these business assets, were funds of the Candidate.

RRFC representatives also contended that subchapter S corporations are synonymous with sole proprietorships, and the earnings of the subchapter S corporations are income to the Candidate. Therefore, RRFC representatives argue that these corporate earnings represent personal income of the Candidate. Subsequently, RFCC Counsel stated that the Candidate's loans to RRFC were funded by the repayment of loans made by the Candidate to the corporations. No documentation to support that statement was provided at that time.

In Matters Under Review (MUR) 3119 involving a similar matter, the Commission maintained that subchapter S corporations are not differentiated from other corporations under the Act. The Commission adopted the position that "although [the corporation] is treated as an S corporation for tax purposes, it remains a corporation for purposes of the Federal Election Campaign Act ("the Act"). The tax ramifications of an S corporation do not remove the funds from corporate control." The Commission concluded that "to view the [corporation] funds as personal rather than corporate funds...solely based on tax consequences to the shareholder – would erode the clear meaning of the statute at Section 441b and go far beyond the Commission's consistent application of Section 441b to all corporations regardless of their structure and purpose."

Prior to issuance of the Interim Audit Report, the Audit staff met with RRFC representatives on several occasions in an effort to resolve this matter as well as to clarify the documentation needed. To further assist RRFC representatives, all meetings were conducted at their legal counsel's office. During this process, RRFC representatives revised their characterization of the source of the Candidate's funds for many of these transactions. Many of the transactions previously described as "distributions" from the subchapter S corporations or "proceeds" from the sale of business assets are now characterized as loan repayments to the Candidate. This evolving characterization of the source of the funds necessitated the Audit staff's requests for additional documentation.

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<sup>7</sup> The sale price for the 50% interest in the business was approximately one-half the amount loaned to the RRFC during 2001.

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### **Interim Audit Report Recommendation**

The Audit staff recommended that RRFC provide evidence demonstrating that the loans to RRFC (\$585,090) were made from the Candidate's personal funds. Complete copies of the 2001 and 2002 tax returns, including supporting schedules, for the Candidate and each of the corporations that transferred funds to the Candidate were requested. Also, copies of bank statements for the Candidate and each corporation for the period June 1, 2001 to December 31, 2002 were requested. In addition, any other evidence needed to:

- Demonstrate how the disbursements made to the Candidate from the subchapter S corporations (except salary payments) were recorded in the accounting records of the corporations.
- Demonstrate how each payment (except salary payments) from the subchapter S corporations to the Candidate during calendar years 2001 and 2002 were accounted for by the Candidate on his tax returns.
- Demonstrate the monthly financial position (i.e. net earnings statements, balance sheets, etc.) of each corporation from August 2001 through June 2002.
- Demonstrate that any payments from the subchapter S corporations to the Candidate, that are not included on the Candidate's tax return as income, represent the return of invested capital, the distributions of previously taxed but undistributed earnings, or the repayment of loans made by the Candidate.
- Demonstrate the sale of his interest in any of the corporations including the purchaser, the price and how the value of the interest sold was determined.

Absent such evidence, the Audit staff further recommended that RRFC repay the outstanding balance of the loans and provide evidence of all repayments (copies of the front and back of the negotiated repayment checks); and, amend its reports to correctly disclose the source of these loans as the corporations.

Prior to the response to the Interim Audit Report, RRFC requested a meeting with the Audit staff to discuss the issues presented in the report. That meeting occurred on February 25, 2004. At that meeting additional documentation was provided, most significantly, the tax returns filed for each of the corporations and the Candidate for the years 2001 and 2002. After reviewing that material, additional questions were raised and on February 27, 2004, additional records were requested. Those records included:

- Documentation to support that the owner of the 26 acres sold in Elgin, AZ was the Candidate rather than Renzi Vino, Inc., an Arizona corporation, as indicated by the documentation supplied (The sale of this property was listed as the source of some of the funds supplied by the Candidate);
- A general ledger transaction report for each corporate entity that lists all transactions, between January 1, 2001 and June 30, 2002, involving transfers of funds to the Candidate and transfers of funds from the Candidate, or a reconciliation of these transactions to the

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lines on which they appear on each corporate tax return (for example, lines 14 (Other Assets) and 19 (Loans from Shareholders) of Schedule L, Form 1120S)<sup>8</sup>; and,

- Bank statements and copies of deposits and checks that support those entries provided on the transaction reports requested above, for which this documentation has not been provided. If copies of specific deposit items and checks were not readily available, they should be submitted as soon as possible after the response to the Interim Audit Report is due.

### **Committee Response to Interim Audit Report**

In its response to the Interim Audit Report, RRFC details the documentation that has been made available for the Audit staff's review; or, for which copies were provided to address the source of the Candidate loans. The response emphasizes RRFC's commitment to working with the Audit staff in resolving this matter and states that they are continuing to search for the additional documentation requested by the Audit staff. It should be noted that only a portion of the documentation requested in the Interim Audit Report was provided and none that was included in the follow-up request.

The response notes that a federal candidate is permitted to make unlimited contributions and loans from personal funds to his authorized committee. It cites 11 CFR §110.10(b) which defines personal funds as:

- Any assets which, under applicable state law, at the time he or she became a candidate, the candidate had a legal right of access to or control over, and with respect to which the candidate had either; legal and rightful title, or an equitable interest; and,
- Salary and other earned income from a bona fide employment and dividends and proceeds from the sale of the candidate's stocks or other investments.

The response continues by citing Title 26, Subtitle A, Chapter 1, Subchapter S of the Internal Revenue Code. This chapter states that a small business corporation, including one owned by a single shareholder may elect to have its income or loss passed through and taxed to its shareholder as ordinary income to avoid double taxation.

RRFC's response also cites MURs 5283 and 5285 to demonstrate that the Commission found no violation where loans were made by a candidate from the proceeds of distributions to the Candidate from a subchapter S corporation. In that case, the distributions to the Candidate were authorized by the corporate board of directors and the funds consisted of previously taxed earnings that had been left with the corporation for working capital. The response also cites MURs 3119 and 3191 as examples where funds borrowed from the general treasury of the corporation were the source of funds for campaign loans made by the Candidate. In reaching its conclusion, the Commission noted that "the money provided to [the candidate] in this matter originated directly from [the corporation's] general treasury funds in the forms of loans which

<sup>8</sup> The tax returns presented reflect balances on lines that record amounts owed to and amounts owed by shareholders. In addition, in some cases the amounts owed to corporations by the Candidate or owed to the Candidate by corporations were recorded on other lines, such as Schedule L line 14 (Other Assets).

27044160482

[the candidate] was required to satisfy, thus evidencing that these funds were controlled by [the corporation] and not [the candidate].”

In summation, the response notes that the loans were made using the Candidate’s personal funds as defined under Commission regulations and precedents, not corporate funds. RRFC maintained that the Candidate either used: distributions from the S corporations, loan repayments received from the S corporations or the proceeds from the sale of assets to make loans during the campaign period. All these monies satisfied the standards cited in the above-noted MURs for determining source of funds were personal funds of the candidate. The Candidate retained sole interest in the funds; the corporations did not retain any interest in or otherwise control the funds. As a result, the Candidate was not required to repay the monies to the corporations. The response concludes that Mr. Renzi’s personal assets were the original source of funds arising from the second mortgage and the sale of 50% equity in Fountain Realty & Development, Inc. Further, the proceeds of the sale of the 26 acres in Elgin, Arizona were disclosed on the Candidate’s personal tax returns. RRFC maintained that the Candidate, in his capacity as a small business owner, used his personal assets to make loans to his companies that were eventually repaid to him.

#### **Audit Staff’s Assessment of Committee Response**

The interim audit report questioned the permissibility of the funds used by the Candidate to make loans totaling \$585,090 to RRFC. In its response to the interim report, RRFC provides an explanation that concludes that the entire amount represents the Candidate’s personal funds. Some is characterized as profit distributions, some as the repayment of loans made to the corporations with personal funds, and some as the sale of personal assets. A thorough review of all available documentation lead the Audit staff to conclude that loans to RRFC totaling \$216,000 likely were made with permissible funds, while loans totaling \$369,090 were made using impermissible corporate funds. In reaching this conclusion each transaction was compared to the documentation submitted and to copies of the personal and corporate tax returns. In a number of cases, the tax returns did not support the explanations and other documentation provided. In those cases, the Audit staff relied on the characterizations contained on the tax returns.

As noted above, part of RRFC’s response relies on several MURs. In those MURs where the funds used by the candidate were the distribution of previously taxed but undistributed earnings, the Commission found no violation. In other cases where the funds used were determined to be corporate treasury funds, a violation was found. With respect to \$369,090 discussed below, the Audit Staff concludes that the situation is analogous to those instances where the Commission found violations.

Our detailed analysis of the documentation provided by RRFC is presented below. The transactions are discussed, grouped by year and by the entity that was the source of the funds: Renzi & Co., Inc. [\$464,090 (\$394,090 in 2001 and \$70,000 in 2002)]; and Fountain Realty & Development, Inc. [\$121,000 (\$10,000 in 2001 and \$111,000 in 2002)].

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- **Renzi & Co., Inc. 2001**

The Audit staff's review of the documentation provided by RRFC indicates that the Candidate deposited a total of \$388,015 into an account of Renzi & Co., Inc. during 2001. No similar transactions are shown in 2002. The deposited monies consisted of:

- a 2<sup>nd</sup> mortgage on the Candidate's home (\$163,015) deposited August 29, 2001 and recorded as "Other Inc:Proceeds" with a memo indicating that the amount was a loan from the Candidate;
- a portion of the proceeds from the sale of the Candidate's 50% interest in Fountain Realty & Development, Inc.. On October 11, 2001, \$100,000 was deposited and recorded as "Other Inc:Proceeds" and on October 25, 2001, \$25,000 was deposited and recorded as "Personal Loan From Rick". Both entries have memo notations that state the amounts are loans from the Candidate and are associated with the sale of his interest in Fountain Realty and Development, Inc.. In addition, proceeds from this sale, originally deposited to Fountain Realty & Development, Inc. were transferred the same day as the deposits to Renzi & Co., Inc. (\$50,000 on October 3, 2001 and \$15,000 on October 10, 2001). In Fountain Realty and Development, Inc.'s accounting records the amounts are recorded as "Other Inc:Proceeds" with memos stating that the amounts were loans from the Candidate and are associated with the sale. RRFC provided no documentation to support how the transferred amounts are recorded in Renzi & Co., Inc.'s accounting records or why the transfers were made. The respective corporate tax returns do not detail an obligation of Renzi & Co., Inc. to Fountain Realty & Development, Inc. at either the beginning or end of the tax year; and,
- monies from the sale of the 26 acres in Elgin, Arizona (\$35,000) deposited on December 27, 2001. Although, settlement records and local land records show that this property was held in the name of Renzi Vino, Inc. an Arizona corporation, the gain from the sale was reported on the Candidate's tax return. The deposit of the \$35,000 is recorded in the Renzi & Co., Inc. accounting records as "Other Inc:Proceeds" with a memo that explains that it is the down payment from the sale. The payment to the Candidate the next day is recorded as "Loan Repayment/Rick". According to RRFC, the \$35,000 was simply deposited in the Renzi & Co., Inc. account to earn interest at a higher rate, and then transferred to the Candidate's account the next day (December 28, 2001). The difference in interest earned on \$35,000 for one day would be negligible. However, given the tax treatment of the funds, it appears to be the equivalent of a distribution from the corporation.

Although the Audit staff agrees that the monies deposited with Renzi & Co., Inc., as discussed above, represent the Candidate's personal funds, it is not clear that the funds represent loans to Renzi & Co. RRFC has asserted that these monies represent loans from the Candidate to Renzi & Co., Inc.; and that, the payments made by Renzi & Co., Inc. to the Candidate, totaling \$394,500, represent repayments of these loans. RRFC concludes

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that these loan repayments therefore represent personal funds of the Candidate. The Audit staff agrees that the repayment of loans made by the Candidate from his personal funds to the corporation represent the Candidate's personal funds. However, while some of the documentation made available to the Audit staff suggests that the payments to the Candidate represent loan repayments, other materials suggest that the funds deposited into Renzi & Co., Inc. accounts may have been in partial satisfaction of loans that the Candidate received from the business and that the money paid to the Candidate represents additional borrowing.

In support of its position, RRFC presented heavily redacted printouts from Renzi and Co., Inc.'s accounting system showing that \$323,015 was either recorded by Renzi & Co., Inc. as loans from the Candidate or had associated memos that suggest that the amounts were loans by the Candidate. However, the tax returns provided do not support this characterization. Incorporated in the IRS Form 1120S (tax return of a Subchapter S Corporation), is a statement of assets and liabilities (Schedule L, Balance Sheet Per Books) for both the beginning and end of the tax year. Documentation provided by RRFC indicated that, during 2001, payments totaling \$394,500 were made to the Candidate and recorded as loan repayments. Based on these transactions, at the end of 2001, Renzi & Co., Inc. had made loan repayments that exceeded the amount loaned by \$71,485 (\$394,500 – \$323,015<sup>11</sup>). The 2001 and 2002 1120S tax returns for Renzi & Co., Inc. did not report any liability for "Loans from Shareholders" or any amounts owed to the Candidate among other liabilities at the beginning or end of either year. Further, the Candidate's schedule K-1 (Shareholder's Share of Income, Credits, Deductions, etc.) for 2001 has no entry for line 21 (Amount of loan repayments for "Loans From Shareholders"). Because the tax returns do not show all of the transactions that affect the reported balances and given that the available documentation suggests that the loans and repayments were not equal during the year, a balance would be expected at the beginning or end of the year, or perhaps both, and an amount would be expected under loan repayments<sup>12</sup>.

On the contrary, among the assets shown on the Balance Sheet are notes receivable from the Candidate that shows the Candidate owed Renzi & Co. considerably more than the amounts at issue here. In 2001, the amount owed by the Candidate increased by approximately \$186,000; and, in 2002, decreased by about \$19,000. Thus rather than the tax returns supporting the representation that the Candidate loaned Renzi & Co., Inc. money during 2001 and received repayments, it appears that the Candidate had previously borrowed money from the corporation and borrowed additional amounts during 2001. The records presented to date do not establish that \$359,090 of the \$394,090 in loans arising in 2001 represent the Candidate's personal funds. The remaining \$35,000, from the sale of the land appears permissible.

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<sup>11</sup> The \$65,000 transferred from Fountain Realty & Development is not included in this figure since RRFC provided no documentation to show it was recorded as a loan from the Candidate. If it were included, the difference between amounts from the Candidate deposited and amounts paid to the Candidate would be only \$6,485.

<sup>12</sup> On the tax return of Fountain Realty & Development, amounts owed to the Candidate are recorded at the beginning and end of 2002, and the line on the tax return that reflects loan repayments to shareholders is filled in.

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RRFC disclosure reports indicate that with respect to the \$35,000 loan, \$25,000 was repaid on November 4, 2002 and the balance (\$10,000) remained outstanding through August 18, 2004. The remaining loans during 2001 (\$359,090) were reduced by: \$70,000 on January 30, 2002; \$140,000 on October 7, 2002; \$64,000 on October 17, 2002; \$2,500 on December 20, 2002; and \$12,500 during 2003. The balance of \$70,090 remains outstanding as of August 18, 2004.

- **Fountain Realty & Development, Inc. (formerly Renzi Investments, Inc.) 2001**

As noted above, a total of \$75,000 was deposited into the account of Fountain Realty & Development, Inc. on October 3, 2001 (\$50,000) and October 10, 2001 (\$25,000). Also as noted above, the deposits were recorded differently, but each had an associated memo that states the amounts were loans from the Candidate and that the funds were associated with the Candidate's sale of part of his interest in the business. According to the 2001 tax return of Fountain Realty & Development, Inc., the balance in the Loans From Shareholders account increased by a slightly larger amount during 2001. Of the \$75,000 loaned to Fountain Realty & Development, Inc., \$65,000 was immediately transferred to Renzi & Co., Inc. and is part of the funds discussed above. The remaining \$10,000 arising from this sale remained with Fountain Realty & Development, Inc.

RRFC's response states that the Candidate also received a \$10,000 distribution from Fountain Realty & Development, Inc. Although RRFC states the \$10,000 distribution was the source of funds for a loan to RRFC, the documentation presented by RRFC does not support this transfer of funds as a "distribution". The 2001 tax return for Fountain Realty & Development, Inc. and the Candidate's personal tax return show taxable income from Fountain Realty & Development, Inc. However taxable income is not synonymous with cash distributions. The Fountain Realty & Development, Inc. tax return does not report any cash distributions to the candidate, any loan repayments to the Candidate, or any corresponding non-deductible expense.<sup>9</sup> Furthermore, this transaction was recorded by Fountain Realty & Development, Inc. as a "Personal Expense". The records presented to date do not establish that the \$10,000 payment to the Candidate represents his personal funds. This \$10,000 loan was repaid October 17, 2002.

- **Renzi & Co., Inc. 2002 (now Patriot Insurance Agency, Inc.)**

During 2002, RRFC states that the Candidate received a \$70,000 distribution from Renzi & Co., Inc. on March 28, 2002, which was recorded as "Transfer to Rick Personal". RRFC once again references the line on the Candidate's tax return that is used to report his portion of the business income but does not reflect cash distributions. However, Renzi & Co.'s tax return for 2002 and the Candidate's Schedule K-1 report that distributions well in excess of \$70,000 were made during the year. The total distributions were less than Renzi & Co.'s income for the year. It is therefore accepted that the

<sup>9</sup> Neither Line 7 of Schedule M-2 from Form 1120S (Distributions other than dividend distributions) or Line 20 of Schedule K-1 from Form 1120S (Property distributions...) report a distribution. Also, the change in Retained Earnings between the beginning and end of 2001 on Renzi Investments, Inc. tax return is equal to income reported by the Candidate on his tax return (except for a \$25 non-deductible expense amount) further suggesting that there were no distributions during the year.

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distributions in 2002 represent the Candidate's personal funds<sup>10</sup>. This \$70,000 was part of \$130,000 in loans made by the Candidate to RRFC on March 28, 2002. The remaining \$60,000 is discussed below. This loan (\$70,000) remained outstanding through August 18, 2004, based on the latest disclosure report filed by RRFC.

- **Fountain Realty & Development, Inc. 2002**

In response to the Interim Audit Report, RRFC explains that in late January 2002, RRFC repaid the Candidate \$70,000 that it had borrowed in 2001. The Candidate, in turn, loaned Fountain Realty & Development, Inc. \$70,000 to cover business obligations. On March 14, 2002, Fountain Realty and Development, Inc. repaid the \$70,000 to the Candidate. An affidavit from the Vice President of Fountain Realty & Development, Inc., attesting to these transactions, was provided as evidence. In addition, bank statements for the Candidate and Fountain Realty and Development, Inc. are provided along with some of the associated checks and deposit tickets. When the \$130,000 in loans was made on March 28, 2002, much of this money was still in the Candidate's personal account.<sup>11</sup> It is therefore concluded that the source of \$60,000 (of the \$130,000 loaned on March 28, 2002) was the repayment from Fountain Realty and Development, Inc. However, since the permissibility of much of the money loaned to RRFC in 2001 remains in question, having RRFC repay a portion of those funds, having the Candidate loan it to one of the businesses, having the business repay the Candidate and then return the money to RRFC does not render the funds permissible. However, to include these funds in the impermissible funds in both years would constitute a double count.

RRFC also characterizes a \$51,000 payment to the Candidate on June 28, 2002 as a "loan repayment". Although no detailed documentation was provided that established the original loan from the Candidate to Fountain Realty and Development, Inc., the corporate tax returns indicate significant amounts owed to the Candidate. The corporate tax returns also indicate that the Candidate received \$125,000 in loan repayments during 2002. It should be noted again that, prior to RRFC's submission of their response to the Interim Audit Report, the Audit staff requested a separate general ledger transaction report for each corporate entity that lists all transactions involving transfers of funds to and from the Candidate. RRFC still has not complied with this request. Nonetheless, it is accepted that the \$51,000 payment from Fountain Realty and Development, Inc. represents the personal funds of the Candidate.

These loans (\$130,000) remained outstanding through August 18, 2004, based on the latest disclosure report filed by RRFC.

### **Audit Staff's Conclusion**

The Audit staff concludes that, with respect to the \$464,090 in loans to RRFC arising from Renzi & Co., Inc.:

<sup>10</sup> Without additional corporate records it is not possible to determine if the \$70,000 is a portion of the cash distributions for the year or was made for another purpose.

<sup>11</sup> There were no other deposits between March 14, 2002 and March 28, 2002 when the \$70,000 from Renzi & Co., Inc. discussed above was deposited. The balance in the account prior to the Renzi & Co., Inc. deposit was approximately \$63,000.

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- The \$70,000 loan made during 2002 and \$35,000 loaned to RRFC during 2001 from the sale of real estate were likely made with permissible funds; and
- The remaining \$359,090 in loans arising during 2001 was made with impermissible funds.

The Audit staff concludes that, with respect to the loans of \$121,000 to RRFC arising from Fountain Reality and Development, Inc.:

- The \$51,000 loaned in 2002 was made with permissible funds and the remaining \$60,000 loaned during 2002 has been excluded from the analysis for the reasons stated above; and,
- The \$10,000 loan made during 2001 was made with impermissible funds.

In summation, of the \$585,090 in loans from the Candidate:

- Loans totaling \$156,000 appear to have been made with permissible funds,
- Loans totaling \$60,000 have been excluded as duplicative; and
- Loans totaling \$369,090 were made using impermissible corporate funds.

## **Finding 2. Misstatement of Financial Activity**

### **Summary**

When RRFC's reported activity was compared to its bank records, the Audit staff found that, for calendar year 2002, receipts, disbursements and cash on hand at 12/31/02 had been misstated. In response to the interim audit report, RRFC filed amended reports which materially corrected the misstatements noted above.

### **Legal Standard**

**Contents of Reports.** Each report must disclose:

- The amount of cash on hand at the beginning and end of the reporting period;
- The total amount of receipts for the reporting period and for the election cycle; and
- The total amount of disbursements for the reporting period and for the election cycle.

2 U.S.C. §434(b)(1), (2) and (4).

### **Facts and Analysis**

The following chart details the discrepancies between RRFC's reported activity and its bank records. Succeeding paragraphs explain why the discrepancies occurred.

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2002 Campaign Activity			
	Reported	Bank Records	Discrepancy
Cash on Hand at 01/01/02	\$396,887	\$396,887	\$0
Receipts	\$1,214,965	\$1,252,504	\$37,539 Understated
Disbursements	\$1,549,905	\$1,651,010	\$101,105 Understated
Cash on Hand at 12/31/02	\$61,947	(\$1,619)	\$63,566 Overstated

The understatement of receipts was the net result of the following:

- |                                   |          |
|-----------------------------------|----------|
| • Failure to report contributions | \$38,875 |
| • Reporting contribution twice    | ( 500)   |
| • Unexplained differences         | ( 836)   |
|                                   | \$37,539 |

The understatement of disbursements was the net result of the following:

- |   |           |
|---|-----------|
| • Failure to report disbursements                         | \$123,734 |
| • Reporting disbursements without supporting bank records | ( 22,344) |
| • Unexplained differences                                 | ( 285)    |
|   | \$101,105 |

The overstatement of the closing cash on hand was the net result of the misstatements described above.

The Audit staff discussed this matter with RRFC representatives at the exit conference and supplied them with schedules detailing the discrepancies noted above. RRFC representatives stated that they would amend the appropriate schedules as necessary.

#### **Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that RRFC amend its reports to correct the misstatements noted above. In response to the interim audit report, RRFC amended its reports to materially correct the misstatements noted above.

### **Finding 4. Disclosure of Transfers from Authorized Committees**

#### **Summary**

RRFC did not disclose transfers of joint fundraising proceeds totaling \$134,495. In response to the interim audit report, RRFC filed amended reports to disclose these receipts correctly.

#### **Legal Standard**

**Reporting of Receipts.** After receiving proceeds of a joint fundraiser, each participating committee must report:

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- Its share of net proceeds received as a transfer-in from the fundraising representative; and
- Its share of gross receipts from each contributor as memo entries. 11 CFR §102.17(c)(8)(i)(B).

**Identification.** In the case of an individual, his or her full name, including: First name, middle name or initial (if available), and last name; mailing address; occupation; and the name of his or her employer. 11 CFR §100.12.

### **Facts and Analysis**

RRFC received three transfers from The Leadership Committee (TLC) totaling \$134,495. TLC is listed on RRFC's Statement of Organization as an affiliated committee with a relationship as a joint fundraising representative. None of the transfers were disclosed on Schedule A, Line 12 (Transfers from Other Authorized Committees). Furthermore, memo entries disclosing individuals who gave in excess of \$200, or political committees that contributed any amount, were not provided for any of the three transfers as required. Rather, RRFC reported the individual and political committee contributions that made up the transfers on Schedules A for Line 11.

At the exit conference, the Audit staff discussed this matter with RRFC representatives and provided a schedule detailing the transfers from TLC that were not disclosed. To correct these errors, RRFC representatives agreed to amend Schedules A for Line 12 to properly disclose these transfers from an authorized committee.

### **Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that RRFC file amended reports to accurately disclose the transfers from its authorized committee. The amendments should disclose the entire transfer amount on Schedule A, Line 12 and include memo entries for each individual, whose contribution(s) aggregated in excess of \$200, and for each contribution from a political committee comprising the transfer. In response to the interim audit report, RRFC filed the necessary reports for 2002 that correctly disclosed these transfers.

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## Report of the Audit Division on Rick Renzi for Congress

December 18, 2001 – December 31, 2002

### Why the Audit Was Done

Federal law permits the Commission to conduct audits and field investigations of any political committee that is required to file reports under the Federal Election Campaign Act (the Act). The Commission generally conducts such audits when a committee appears not to have met the threshold requirements for substantial compliance with the Act.<sup>1</sup> The audit determines whether the committee complied with the limitations, prohibitions and disclosure requirements of the Act.

### Future Action

The Commission may initiate an enforcement action, at a later time, with respect to any of the matters discussed in this report

### About the Campaign (p. 2)

Rick Renzi for Congress (RRFC) is the principal campaign committee for Richard G. Renzi, Republican candidate for the U.S. House of Representatives from the state of Arizona, First District. RRFC is headquartered in Flagstaff, Arizona. For more information, see chart on the Campaign Organization, p. 2.

### Financial Activity (p. 2)

- Receipts
  - From Individuals \$ 362,736
  - From Political Committees 527,605
  - Candidate Loans 763,090
  - Other Receipts 3,163
  - Total Receipts \$ 1,656,594
- Disbursements
  - Operating & Other Disbursements \$ 1,658,213
  - Total Disbursements \$1,658,213

### Findings and Recommendations (p. 3)

- Apparent Corporate Contributions (Finding 1)
- Misstatement of Financial Activity (Finding 2)
- Reporting of Contributions from Political Committees (Finding 3)
- Disclosure of Transfers from Authorized Committees (Finding 4)
- Disclosure of Occupation and Name of Employer (Finding 5)

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<sup>1</sup> 2 U.S.C. §438(b)

# **Report of the Audit Division on Rick Renzi for Congress**

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December 18, 2001 – December 31, 2002



# Table of Contents

	Page
<b>Part I. Background</b>	
Authority for Audit	1
Scope of Audit	1
Changes to the Law	1
<b>Part II. Overview of Campaign</b>	
Campaign Organization	2
Overview of Financial Activity	2
<b>Part III. Summaries</b>	
Findings and Recommendations	3
<b>Part IV. Findings and Recommendations</b>	
Finding 1. Apparent Corporate Contributions	4
Finding 2. Misstatement of Financial Activity	14
Finding 3. Reporting of Contributions from Political Committees	15
Finding 4. Disclosure of Transfers from Authorized Committees	16
Finding 5. Disclosure of Occupation and Name of Employer	17



# Part I

## Background

### Authority for Audit

This report is based on an audit of Rick Renzi for Congress (RRFC), undertaken by the Audit Division of the Federal Election Commission (the Commission) in accordance with the Federal Election Campaign Act of 1971, as amended (the Act). The Audit Division conducted the audit pursuant to 2 U.S.C. §438(b), which permits the Commission to conduct audits and field investigations of any political committee that is required to file a report under 2 U.S.C. §434. Prior to conducting any audit under this subsection, the Commission must perform an internal review of reports filed by selected committees to determine if the reports filed by a particular committee meet the threshold requirements for substantial compliance with the Act. 2 U.S.C. §438(b).

### Scope of Audit

Following Commission approved procedures, the Audit staff evaluated various factors and as a result, this audit examined:

1. The receipt of excessive contributions and loans.
2. The receipt of contributions from prohibited sources.
3. The disclosure of contributions received
4. The consistency between reported figures and bank records
5. The completeness of records.
6. Other committee operations necessary to the review

### Changes to the Law

On March 27, 2002, President Bush signed into law the Bipartisan Campaign Reform Act of 2002 (BCRA). The BCRA contains many substantial and technical changes to the federal campaign finance law. Most of the changes became effective November 6, 2002. Except for November 7, 2002 through December 31, 2002, the period covered by this audit pre-dates these changes. Therefore, the statutory and regulatory requirements cited in this report are primarily those that were in effect prior to November 7, 2002

## Part II

### Overview of Campaign

#### Campaign Organization

<b>Important Dates</b>	<b>Rick Renzi for Congress</b>
• Date of Registration	December 28, 2001
• Audit Coverage	December 18, 2001 through December 31, 2002
<b>Headquarters</b>	Flagstaff, Arizona
<b>Bank Information</b>	
• Bank Depositories	1
• Bank Accounts	1 Checking, 1 Money Market Savings
<b>Treasurer</b>	
• Treasurer When Audit Was Conducted	David W. Dickman
• Treasurer During Period Covered by Audit	William Constantine (through June 30, 2002); David W. Dickman (from July 1, 2002)
<b>Management Information</b>	
• Attended FEC Campaign Finance Seminar	No
• Used Commonly Available Campaign Management Software Package	Yes
• Who Handled Accounting, Recordkeeping Tasks and Other Day-to-Day Operations	Joe Galli until October 2002, after which volunteer staff assumed these tasks

#### Overview of Financial Activity (Audited Amounts)

<b>Cash on hand @ December 18, 2001</b>	<b>\$ 0</b>
<b>Receipts</b>	
o From Individuals	\$362,736
o From Political Committees	527,605
o Candidate Loans	763,090
o Other Receipts	3,163
<b>Total Receipts</b>	<b>\$ 1,656,594</b>
<b>Disbursements</b>	
o Operating & Other Disbursements	\$1,658,213
<b>Total Disbursements</b>	<b>\$ 1,658,213</b>
<b>Cash on hand @ December 31, 2002</b>	<b>(\$ 1,619)<sup>2</sup></b>

<sup>2</sup> The RRFC's reported cash balance on 12/31/02 was significantly misstated, see Finding 2. The negative balance represents a "book" balance, its bank account balances were never negative.

## Part III

### Summaries

#### Findings and Recommendations

##### **Finding 1. Apparent Corporate Contributions**

During the campaign, the Candidate made 11 loans to RRFC totaling \$585,090 which appeared to have originated from corporate accounts. In response to the interim audit report, RRFC maintained that all loans from the Candidate were made utilizing personal funds. RRFC submitted various documents in support of its position. Based on the documentation submitted, it appears that loans of \$369,090 were made using impermissible corporate funds. (For more detail, see p. 4)

##### **Finding 2. Misstatement of Financial Activity**

When RRFC's reported activity was compared to its bank records, the Audit staff found that, for calendar year 2002, receipts, disbursements and cash on hand at 12/31/02 had been misstated. In response to the interim audit report, RRFC filed amended reports which materially corrected the misstatements noted above. (For more detail, see p. 14)

##### **Finding 3. Reporting of Contributions from Political Committees**

RRFC did not itemize thirteen contributions from political committees totaling \$20,745. In response to the interim audit report, RRFC filed amended reports which materially disclosed the receipts noted above. (For more detail, see p. 15)

##### **Finding 4. Disclosure of Transfers from Authorized Committees**

RRFC did not disclose transfers of joint fundraising proceeds totaling \$134,495. In response to the interim audit report, RRFC filed amended reports to disclose these receipts correctly. (For more detail, see p. 16)

##### **Finding 5. Disclosure of Occupation and Name of Employer**

RRFC did not adequately disclose occupation and name of employer information for 200 contributions from individuals totaling \$132,811. No "best efforts" to obtain, maintain and submit this information was demonstrated by RRFC. In response to the interim audit report, RRFC materially complied by filing amended reports disclosing 69% of the missing contributor information. (For more detail, see p. 17)

## Part IV

# Findings and Recommendations

### Finding 1. Apparent Corporate Contributions

#### Summary

During the campaign, the Candidate made 11 loans to RRFC totaling \$585,090 which appeared to have originated from corporate accounts. In response to the interim audit report, RRFC maintained that all loans from the Candidate were made utilizing personal funds. RRFC submitted various documents in support of its position. Based on the documentation submitted, it appears that loans of \$369,090 were made using impermissible corporate funds.

#### Legal Standard

**A. Corporate Contributions Impermissible** A corporation is prohibited from making any contribution in connection with a federal election. 2 U.S.C. §441b(a).

**B. Receipt of Prohibited Contributions – General Prohibition** Candidates and committees may not accept contributions (in the form of money, in-kind contributions or loans):

1. In the name of another; or
2. From the treasury funds of the following prohibited sources
  - Corporations (this means any incorporated organization, including a non-stock corporation, an incorporated membership organization, and an incorporated cooperative),
  - Labor Organizations,
  - National Banks;
  - Federal Government Contractors (including partnerships, individuals, and sole proprietors who have contracts with the federal government); and
  - Foreign Nationals (including individuals who are not U.S. citizens and not lawfully admitted for permanent residence, foreign governments and foreign political parties; and groups organized under the laws of a foreign country or groups whose principal place of business is in a foreign country, as defined in 22 U.S.C. §611(b)) 2 U.S.C. §§441b, 441c, 441e, and 441f.

**C. Definition of Personal Funds** Personal funds include salary and other earned income from bona fide employment and dividends and proceeds from the sale of the candidate's stock or other investments. 11 CFR §110.10(b)(2).

#### Facts and Analysis

The Audit staff reviewed \$763,090 in loans reported by RRFC as made by the Candidate. The Candidate loaned RRFC \$404,090 during December of 2001, and the remaining \$359,000 was loaned throughout 2002.

The Audit staff reviewed the source of funds for all the Candidate loans and determined that \$585,090<sup>3</sup> appeared to have been funded with monies from the following corporations:

- Renzi & Co., Inc.<sup>4</sup>, a subchapter S corporation<sup>5</sup> in which the Candidate held a 90% interest; and
- Fountain Realty and Development, Inc. (formerly Renzi Investments, Inc.<sup>6</sup>), a subchapter S corporation in which the Candidate held a 50% controlling interest

During the audit fieldwork, the Audit staff reviewed selected bank statements, canceled checks, and other documents provided by RRFC, the Candidate, and the corporations. In addition, portions of the 2001 tax returns for the Candidate and the corporations<sup>7</sup> were reviewed. Our analysis of the documents available when the interim audit report was prepared indicated:

- The loans were made by check drawn on the corporate accounts, deposited into the Candidate's personal bank account, and then transferred by wire or check to RRFC's bank account
- None of the checks drawn by the corporations to the Candidate indicated they were distributions of income to the Candidate

In addition, documentation was not provided to establish how, if at all, the amounts

<sup>3</sup> Two additional loans (\$178,000) arose when RRFC made repayments to the Candidate for some of the corporate loans during October, 2002. The Candidate deposited those funds into his personal bank account and then loaned those funds back to RRFC. Since the original source of the loans was the corporations, adding these loans to the total would constitute a double count. Therefore, these loans (\$178,000) are not considered.

<sup>4</sup> Renzi & Co., Inc. is now known as Patriot Insurance Agency, Inc.

<sup>5</sup> A subchapter S corporation (also called S corporation) is a general corporation that has elected a special tax status with the IRS. Subchapter S corporations are most appropriate for small business owners and entrepreneurs who prefer to be taxed as if they were still sole proprietors or partners. Subchapter S corporations avoid "double taxation" (once at the corporate level and again at the personal level) because all income or loss is reported only once on the personal tax returns of the stockholders. Subchapter S corporations are separate legal entities from its stockholders.

<sup>6</sup> Renzi Investments, Inc., was a subchapter S corporation wholly owned by the Candidate. When the Candidate sold a 50% interest in this entity the name became Fountain Realty & Development, Inc.; which is how the Audit staff will refer to it in this report.

<sup>7</sup> Corporate tax returns were provided for Renzi & Co., Inc. (now Patriot Insurance Agency, Inc.), Renzi Investments, Inc. (now Fountain Realty & Development, Inc.), and Fountain Hills Estates Realty & Construction, Inc. (now Renzi Vino, Inc.). However, documentation was not presented to link Fountain Hills Estates Realty & Construction, Inc. to any of the Candidate loans.

paid to the Candidate and subsequently loaned to RRFC relate to profit distributions

- Although RRFC representatives indicated that the sale of 50% of the Candidate's interest in Fountain Realty & Development, Inc. was a source of funds for some of the loans<sup>9</sup>, the documentation available at that time did not support that representation.

however, the loans were made in December 2001, more than three months after the sale. Bank records for the Candidate, Renzi & Co., Inc. and Fountain Realty & Development, Inc. were provided only for December 2001, and did not establish how and when the proceeds of the sale were received by the Candidate. Other documents detailed the sale of the interest to two individuals; however, no information concerning how the purchase price was determined was provided.

At the exit conference, the Audit staff presented this matter to RRFC representatives. They maintained that the funds in question were generated through the sale of various business assets. They argued that these business entities were owned solely or in majority by the Candidate; therefore, profits from the sale of these business assets, were funds of the Candidate.

RRFC representatives also contended that subchapter S corporations are synonymous with sole proprietorships, and the earnings of the subchapter S corporations are income to the Candidate. Therefore, RRFC representatives argue that these corporate earnings represent personal income of the Candidate. Subsequently, RFCC Counsel stated that the Candidate's loans to RRFC were funded by the repayment of loans made by the Candidate to the corporations. No documentation to support that statement was provided at that time.

In Matters Under Review (MUR) 3119 involving a similar matter, the Commission maintained that subchapter S corporations are not differentiated from other corporations under the Act. The Commission adopted the position that "although [the corporation] is treated as an S corporation for tax purposes, it remains a corporation for purposes of the Federal Election Campaign Act ("the Act"). The tax ramifications of an S corporation do not remove the funds from corporate control." The Commission concluded that "to view the [corporation] funds as personal rather than corporate funds...solely based on tax consequences to the shareholder - would erode the clear meaning of the statute at Section 441b and go far beyond the Commission's consistent application of Section 441b to all corporations regardless of their structure and purpose."

Prior to issuance of the Interim Audit Report, the Audit staff met with RRFC representatives on several occasions in an effort to resolve this matter as well as to clarify the documentation needed. To further assist RRFC representatives, all meetings were conducted at their legal counsel's office. During this process, RRFC representatives revised their characterization of the source of the Candidate's funds for many of these transactions. Many of the transactions previously described as "distributions" from the subchapter S corporations or "proceeds" from the sale of business assets are now characterized as loan repayments to the Candidate. This

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<sup>9</sup> The sale price for the 50% interest in the business was approximately one-half the amount loaned to the RRFC during 2001.

evolving characterization of the source of the funds necessitated the Audit staff's requests for additional documentation.

### **Interim Audit Report Recommendation**

The Audit staff recommended that RRFC provide evidence demonstrating that the loans to RRFC (\$585,090) were made from the Candidate's personal funds. Complete copies of the 2001 and 2002 tax returns, including supporting schedules, for the Candidate and each of the corporations that transferred funds to the Candidate were requested. Also, copies of bank statements for the Candidate and each corporation for the period June 1, 2001 to December 31, 2002 were requested. In addition, any other evidence needed to:

- Demonstrate how the disbursements made to the Candidate from the subchapter S corporations (except salary payments) were recorded in the accounting records of the corporations
- Demonstrate how each payment (except salary payments) from the subchapter S corporations to the Candidate during calendar years 2001 and 2002 were accounted for by the Candidate on his tax returns
- Demonstrate the monthly financial position (i.e. net earnings statements, balance sheets, etc.) of each corporation from August 2001 through June 2002
- Demonstrate that any payments from the subchapter S corporations to the Candidate, that are not included on the Candidate's tax return as income, represent the return of invested capital, the distributions of previously taxed but undistributed earnings, or the repayment of loans made by the Candidate
- Demonstrate the sale of his interest in any of the corporations including the purchaser, the price and how the value of the interest sold was determined

Absent such evidence, the Audit staff further recommended that RRFC repay the outstanding balance of the loans and provide evidence of all repayments (copies of the front and back of the negotiated repayment checks); and, amend its reports to correctly disclose the source of these loans as the corporations

Prior to the response to the Interim Audit Report, RRFC requested a meeting with the Audit staff to discuss the issues presented in the report. That meeting occurred on February 25, 2004. At that meeting additional documentation was provided, most significantly, the tax returns filed for each of the corporations and the Candidate for the years 2001 and 2002. After reviewing that material, additional questions were raised and on February 27, 2004, additional records were requested. Those records included

- Documentation to support that the owner of the 26 acres sold in Elgin, AZ was the Candidate rather than Renzi Vino, Inc., an Arizona corporation, as indicated by the documentation supplied (The sale of this property was listed as the source of some of the funds supplied by the Candidate),
- A general ledger transaction report for each corporate entity that lists all transactions, between January 1, 2001 and June 30, 2002, involving transfers of funds to the Candidate and transfers of funds from the Candidate, or a reconciliation of these transactions to the

lines on which they appear on each corporate tax return

and,

- Bank statements and copies of deposits and checks that support those entries provided on the transaction reports requested above, for which this documentation has not been provided. If copies of specific deposit items and checks were not readily available, they should be submitted as soon as possible after the response to the Interim Audit Report is due.

### **Committee Response to Interim Audit Report**

In its response to the Interim Audit Report, RRFC details the documentation that has been made available for the Audit staff's review, or, for which copies were provided to address the source of the Candidate loans. The response emphasizes RRFC's commitment to working with the Audit staff in resolving this matter and states that they are continuing to search for the additional documentation requested by the Audit staff. It should be noted that only a portion of the documentation requested in the Interim Audit Report was provided and none that was included in the follow-up request.

The response notes that a federal candidate is permitted to make unlimited contributions and loans from personal funds to his authorized committee. It cites 11 CFR §110.10(b) which defines personal funds as:

- Any assets which, under applicable state law, at the time he or she became a candidate, the candidate had a legal right of access to or control over, and with respect to which the candidate had either; legal and rightful title, or an equitable interest; and,
- Salary and other earned income from a bona fide employment and dividends and proceeds from the sale of the candidate's stocks or other investments

The response continues by citing Title 26, Subtitle A Chapter 1, Subchapter S of the Internal Revenue Code. This chapter states that a small business corporation, including one owned by a single shareholder may elect to have its income or loss passed through and taxed to its shareholder as ordinary income to avoid double taxation.

RRFC's response also cites MURs 5283 and 5285 to demonstrate that the Commission found no violation where loans were made by a candidate from the proceeds of distributions to the Candidate from a subchapter S corporation. In that case, the distributions to the Candidate were authorized by the corporate board of directors and the funds consisted of previously taxed earnings that had been left with the corporation for working capital. The response also cites MURs 3119 and 3191 as examples where funds borrowed from the general treasury of the corporation were the source of funds for campaign loans made by the Candidate. In reaching its conclusion, the Commission noted that "the money provided to [the candidate] in this matter originated directly from [the corporation's] general treasury funds in the forms of loans which

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[the candidate] was required to satisfy, thus evidencing that these funds were controlled by [the corporation] and not [the candidate] "

In summation, the response notes that the loans were made using the Candidate's personal funds as defined under Commission regulations and precedents, not corporate funds. RRFC maintained that the Candidate either used distributions from the S corporations, loan repayments received from the S corporations or the proceeds from the sale of assets to make loans during the campaign period. All these monies satisfied the standards cited in the above-noted MURs for determining source of funds were personal funds of the candidate. The Candidate retained sole interest in the funds, the corporations did not retain any interest in or otherwise control the funds. As a result, the Candidate was not required to repay the monies to the corporations. The response concludes that Mr. Renzi's personal assets were the original source of funds arising from the second mortgage and the sale of 50% equity in Fountain Realty & Development, Inc.

RRFC maintained that he Candidate, in his capacity as a small business owner, used his personal assets to make loans to his companies that were eventually repaid to him.

#### **Audit Staff's Assessment of Committee Response**

The interim audit report questioned the permissibility of the funds used by the Candidate to make loans totaling \$585,090 to RRFC. In its response to the interim report, RRFC provides an explanation that concludes that the entire amount represents the Candidate's personal funds. Some is characterized as profit distributions, some as the repayment of loans made to the corporations with personal funds, and some as the sale of personal assets. A thorough review of all available documentation lead the Audit staff to conclude that loans to RRFC totaling \$216,000 likely were made with permissible funds, while loans totaling \$369,090 were made using impermissible corporate funds

As noted above, part of RRFC's response relies on several MURs. In those MURs where the funds used by the candidate were the distribution of previously taxed but undistributed earnings, the Commission found no violation. In other cases where the funds used were determined to be corporate treasury funds, a violation was found. With respect to \$369,090 discussed below, the Audit Staff concludes that the situation is analogous to those instances where the Commission found violations.

Our detailed analysis of the documentation provided by RRFC is presented below. The transactions are discussed, grouped by year and by the entity that was the source of the funds: Renzi & Co., Inc. [\$464,090 (\$394,090 in 2001 and \$70,000 in 2002)]; and Fountain Realty & Development, Inc. [\$121,000 (\$10,000 in 2001 and \$111,000 in 2002)]

• **Renzi & Co., Inc. 2001**

The Audit staff's review of the documentation provided by RRFC indicates that the Candidate deposited a total of \$388,015 into an account of Renzi & Co., Inc. during 2001. No similar transactions are shown in 2002. The deposited monies consisted of:

- a 2<sup>nd</sup> mortgage on the Candidate's home (\$163,015) deposited August 29, 2001 and recorded as "Other Inc:Proceeds" with a memo indicating that the amount was a loan from the Candidate,
- a portion of the proceeds from the sale of the Candidate's 50% interest in Fountain Realty & Development, Inc.. On October 11, 2001, \$100,000 was deposited and recorded as "Other Inc:Proceeds" and on October 25, 2001, \$25,000 was deposited and recorded as "Personal Loan From Rick". Both entries have memo notations that state the amounts are loans from the Candidate and are associated with the sale of his interest in Fountain Realty and Development, Inc. In addition, proceeds from this sale, originally deposited to Fountain Realty & Development, Inc. were transferred the same day as the deposits to Renzi & Co., Inc. (\$50,000 on October 3, 2001 and \$15,000 on October 10, 2001). In Fountain Realty and Development, Inc.'s accounting records the amounts are recorded as "Other Inc:Proceeds" with memos stating that the amounts were loans from the Candidate and are associated with the sale. RRFC provided no documentation to support how the transferred amounts are recorded in Renzi & Co., Inc.'s accounting records or why the transfers were made.
- monies from the sale of the 26 acres in Elgin, Arizona (\$35,000) deposited on December 27, 2001. Although, settlement records and local land records show that this property was held in the name of Renzi Vino, Inc. an Arizona corporation, The deposit of the \$35,000 is recorded in the Renzi & Co., Inc. accounting records as "Other Inc:Proceeds" with a memo that explains that it is the down payment from the sale. The payment to the Candidate the next day is recorded as "Loan Repayment/Rick". According to RRFC, the \$35,000 was simply deposited in the Renzi & Co., Inc. account to earn interest at a higher rate, and then transferred to the Candidate's account the next day (December 28, 2001). The difference in interest earned on \$35,000 for one day would be negligible.

Although the Audit staff agrees that the monies deposited with Renzi & Co., Inc., as discussed above, represent the Candidate's personal funds, it is not clear that the funds represent loans to Renzi & Co. RRFC has asserted that these monies represent loans from the Candidate to Renzi & Co., Inc., and that, the payments made by Renzi & Co., Inc. to

the Candidate, totaling \$394,500, represent repayments of these loans. RRFC concludes that these loan repayments therefore represent personal funds of the Candidate. The Audit staff agrees that the repayment of loans made by the Candidate from his personal funds to the corporation represent the Candidate's personal funds. However, while some of the documentation made available to the Audit staff suggests that the payments to the Candidate represent loan repayments, other materials suggest that the funds deposited into Renzi & Co., Inc. accounts may have been in partial satisfaction of loans that the Candidate received from the business and that the money paid to the Candidate represents additional borrowing.

In support of its position, RRFC presented heavily redacted printouts from Renzi and Co., Inc.'s accounting system showing that \$323,015 was either recorded by Renzi & Co., Inc. as loans from the Candidate or had associated memos that suggest that the amounts were loans by the Candidate.

Documentation provided by

RRFC indicated that, during 2001, payments totaling \$394,500 were made to the Candidate and recorded as loan repayments. Based on these transactions, at the end of 2001, Renzi & Co., Inc. had made loan repayments that exceeded the amount loaned by \$71,485 (\$394,500 - \$323,015<sup>11</sup>)

among the assets shown on the Balance Sheet are notes receivable from the Candidate that shows the Candidate owed Renzi & Co. considerably more than the amounts at issue here. In 2001, the amount owed by the Candidate increased by approximately \$186,000; and, in 2002, decreased by about \$19,000. Thus rather than the tax returns supporting the representation that the Candidate loaned Renzi & Co., Inc. money during 2001 and received repayments, it appears that the Candidate had previously borrowed money from the corporation and borrowed additional amounts during 2001.

<sup>11</sup> The \$65,000 transferred from Fountain Realty & Development is not included in this figure since RRFC provided no documentation to show it was recorded as a loan from the Candidate. If it were included, the difference between amounts from the Candidate deposited and amounts paid to the Candidate would be only \$6,485.

The records presented to date do not establish that \$359,090 of the \$394,090 in loans arising in 2001 represent the Candidate's personal funds. The remaining \$35,000, from the sale of the land appears permissible.

RRFC disclosure reports indicate that with respect to the \$35,000 loan, \$25,000 was repaid on November 4, 2002 and the balance (\$10,000) remained outstanding through August 18, 2004. The remaining loans during 2001 (\$359,090) were reduced by: \$70,000 on January 30, 2002; \$140,000 on October 7, 2002; \$64,000 on October 17, 2002; \$2,500 on December 20, 2002, and \$12,500 during 2003. The balance of \$70,090 remains outstanding as of August 18, 2004.

- **Fountain Realty & Development, Inc. (formerly Renzi Investments, Inc.) 2001**  
As noted above, a total of \$75,000 was deposited into the account of Fountain Realty & Development, Inc. on October 3, 2001 (\$50,000) and October 10, 2001 (\$25,000). Also as noted above, the deposits were recorded differently, but each had an associated memo that states the amounts were loans from the Candidate and that the funds were associated with the Candidate's sale of part of his interest in the business.

Of the \$75,000

loaned to Fountain Realty & Development, Inc., \$65,000 was immediately transferred to Renzi & Co., Inc. and is part of the funds discussed above. The remaining \$10,000 arising from this sale remained with Fountain Realty & Development, Inc.

RRFC's response states that the Candidate also received a \$10,000 distribution from Fountain Realty & Development, Inc. Although RRFC states the \$10,000 distribution was the source of funds for a loan to RRFC, the documentation presented by RRFC does not support this transfer of funds as a "distribution"

this transaction was recorded

by Fountain Realty & Development, Inc. as a "Personal Expense". The records presented to date do not establish that the \$10,000 payment to the Candidate represents his personal funds. This \$10,000 loan was repaid October 17, 2002.

- **Renzi & Co., Inc. 2002 (now Patriot Insurance Agency, Inc.)**  
During 2002, RRFC states that the Candidate received a \$70,000 distribution from Renzi & Co., Inc. on March 28, 2002, which was recorded as "Transfer to Rick Personal". RRFC once again references the line on the Candidate's tax return that is used to report his portion of the business income but does not reflect cash distributions. However,

It is therefore accepted that the distributions in 2002 represent the Candidate's personal funds<sup>14</sup>. This \$70,000 was part of \$130,000 in loans made by the Candidate to RRFC on March 28, 2002. The remaining \$60,000 is discussed below. This loan (\$70,000) remained outstanding through August 18, 2004, based on the latest disclosure report filed by RRFC.

- **Fountain Realty & Development, Inc. 2002**

In response to the Interim Audit Report, RRFC explains that in late January 2002, RRFC repaid the Candidate \$70,000 that it had borrowed in 2001. The Candidate, in turn, loaned Fountain Realty & Development, Inc. \$70,000 to cover business obligations. On March 14, 2002, Fountain Realty and Development, Inc. repaid the \$70,000 to the Candidate. An affidavit from the Vice President of Fountain Realty & Development, Inc., attesting to these transactions, was provided as evidence. In addition, bank statements for the Candidate and Fountain Realty and Development, Inc. are provided along with some of the associated checks and deposit tickets. When the \$130,000 in loans was made on March 28, 2002, much of this money was still in the Candidate's personal account.<sup>15</sup> It is therefore concluded that the source of \$60,000 (of the \$130,000 loaned on March 28, 2002) was the repayment from Fountain Realty and Development, Inc. However, since the permissibility of much of the money loaned to RRFC in 2001 remains in question, having RRFC repay a portion of those funds, having the Candidate loan it to one of the businesses, having the business repay the Candidate and then return the money to RRFC does not render the funds permissible. However, to include these funds in the impermissible funds in both years would constitute a double count.

RRFC also characterizes a \$51,000 payment to the Candidate on June 28, 2002 as a "loan repayment". Although no detailed documentation was provided that established the original loan from the Candidate to Fountain Realty and Development, Inc., the corporate tax returns indicate

It should be noted again that, prior to RRFC's submission of their response to the Interim Audit Report, the Audit staff requested a separate general ledger transaction report for each corporate entity that lists all transactions involving transfers of funds to and from the Candidate. RRFC still has not complied with this request. Nonetheless, it is accepted that the \$51,000 payment from Fountain Realty and Development, Inc. represents the personal funds of the Candidate.

These loans (\$130,000) remained outstanding through August 18, 2004, based on the latest disclosure report filed by RRFC.

<sup>14</sup> Without additional corporate records it is not possible to determine if the \$70,000 is a portion of the cash distributions for the year or was made for another purpose.

<sup>15</sup> There were no other deposits between March 14, 2002 and March 28, 2002 when the \$70,000 from Renzi & Co., Inc. discussed above was deposited. The balance in the account prior to the Renzi & Co., Inc. deposit was approximately \$63,000.

### **Audit Staff's Conclusion**

The Audit staff concludes that, with respect to the \$464,090 in loans to RRFC arising from Renzi & Co., Inc.:

- The \$70,000 loan made during 2002 and \$35,000 loaned to RRFC during 2001 from the sale of real estate were likely made with permissible funds; and
- The remaining \$359,090 in loans arising during 2001 was made with impermissible funds

The Audit staff concludes that, with respect to the loans of \$121,000 to RRFC arising from Fountain Reality and Development, Inc

- The \$51,000 loaned in 2002 was made with permissible funds and the remaining \$60,000 loaned during 2002 has been excluded from the analysis for the reasons stated above, and,
- The \$10,000 loan made during 2001 was made with impermissible funds.

In summation, of the \$585,090 in loans from the Candidate

- Loans totaling \$156,000 appear to have been made with permissible funds,
- Loans totaling \$60,000 have been excluded as duplicative; and
- Loans totaling \$369,090 were made using impermissible corporate funds.

## **Finding 2. Misstatement of Financial Activity**

### **Summary**

When RRFC's reported activity was compared to its bank records, the Audit staff found that, for calendar year 2002, receipts, disbursements and cash on hand at 12/31/02 had been misstated. In response to the interim audit report, RRFC filed amended reports which materially corrected the misstatements noted above.

### **Legal Standard**

**Contents of Reports.** Each report must disclose

- The amount of cash on hand at the beginning and end of the reporting period;
  - The total amount of receipts for the reporting period and for the election cycle; and
  - The total amount of disbursements for the reporting period and for the election cycle.
- 2 U.S.C. §434(b)(1), (2) and (4).

### **Facts and Analysis**

The following chart details the discrepancies between RRFC's reported activity and its bank records. Succeeding paragraphs explain why the discrepancies occurred

2002 Campaign Activity			
	Reported	Bank Records	Discrepancy
Cash on Hand at 01/01/02	\$396,887	\$396,887	\$0
Receipts	\$1,214,965	\$1,252,504	\$37,539 Understated
Disbursements	\$1,549,905	\$1,651,010	\$101,105 Understated
Cash on Hand at 12/31/02	\$61,947	(\$1,619)	\$63,566 Overstated

The understatement of receipts was the net result of the following:

- Failure to report contributions \$38,875
  - Reporting contribution twice ( 500)
  - Unexplained differences ( 836)
- \$37,539

The understatement of disbursements was the net result of the following:

- Failure to report disbursements \$123,734
  - Reporting disbursements without supporting bank records ( 22,344)
  - Unexplained differences ( 285)
- \$101,105

The overstatement of the closing cash on hand was the net result of the misstatements described above.

The Audit staff discussed this matter with RRFC representatives at the exit conference and supplied them with schedules detailing the discrepancies noted above. RRFC representatives stated that they would amend the appropriate schedules as necessary.

#### **Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that RRFC amend its reports to correct the misstatements noted above. In response to the interim audit report, RRFC amended its reports to materially correct the misstatements noted above.

### **Finding 3. Reporting of Contributions from Political Committees**

#### **Summary**

RRFC did not itemize thirteen contributions from political committees totaling \$20,745. In response to the interim audit report, RRFC filed amended reports which materially disclosed the receipts noted above

### **Legal Standard**

#### **A. When to Itemize.** Political committees must itemize

- Every contribution from any political committee, regardless of the amount.
- Every transfer from another political party committee, regardless of whether the committees are affiliated. 2 U S C §434(b)(3)(A), (B) and (D).

#### **B. Definition of Itemization** Itemization of contributions received means that the recipient committee discloses, on a separate schedule, the following information

- The amount of the contribution,
- The date of receipt (the date the committee received the contribution),
- The full name and address of the contributor; and
- The election-to-date (or election cycle-to-date in the case of authorized candidate committees) total of all contributions from the same contributor 11 CFR §§100.12 and 104.3(a)(4) and 2 U.S.C. §434(b)(3)(A) and (B).

### **Facts and Analysis**

The Audit staff reviewed all contributions from political committees. From this review, it was determined that RRFC did not itemize thirteen contributions totaling \$20,745. Of these thirteen contributions, seven were received during the Year-End 2002 reporting period (November 26, 2002 – December 31, 2002). The Audit staff could not determine, nor could RRFC representatives explain, why these contributions were not itemized

The Audit staff discussed this matter with RRFC representatives at the exit conference and provided them with schedules detailing the contributions not reported. RRFC representatives stated they would amend the appropriate schedules as necessary.

### **Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that RRFC amend its reports to disclose the contributions from political committees discussed above. In response to the interim audit report, RRFC filed amended reports that materially corrected the omissions noted by the Audit staff

## **Finding 4. Disclosure of Transfers from Authorized Committees**

### **Summary**

RRFC did not disclose transfers of joint fundraising proceeds totaling \$134,495. In response to the interim audit report, RRFC filed amended reports to disclose these receipts correctly.

### **Legal Standard**

**Reporting of Receipts.** After receiving proceeds of a joint fundraiser, each participating committee must report:

- Its share of net proceeds received as a transfer-in from the fundraising representative; and
- Its share of gross receipts from each contributor as memo entries. 11 CFR §102.17(c)(8)(i)(B)



**Identification** In the case of an individual, his or her full name, including: First name, middle name or initial (if available), and last name, mailing address, occupation, and the name of his or her employer. 11 CFR §100.12

### **Facts and Analysis**

RRFC received three transfers from The Leadership Committee (TLC) totaling \$134,495. TLC is listed on RRFC's Statement of Organization as an affiliated committee with a relationship as a joint fundraising representative. None of the transfers were disclosed on Schedule A, Line 12 (Transfers from Other Authorized Committees). Furthermore, memo entries disclosing individuals who gave in excess of \$200 or political committees that contributed any amount, were not provided for any of the three transfers as required. Rather, RRFC reported the individual and political committee contributions that made up the transfers on Schedules A for Line 11

At the exit conference, the Audit staff discussed this matter with RRFC representatives and provided a schedule detailing the transfers from TLC that were not disclosed. To correct these errors, RRFC representatives agreed to amend Schedules A for Line 12 to properly disclose these transfers from an authorized committee

### **Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that RRFC file amended reports to accurately disclose the transfers from its authorized committee. The amendments should disclose the entire transfer amount on Schedule A, Line 12 and include memo entries for each individual, whose contribution(s) aggregated in excess of \$200, and for each contribution from a political committee comprising the transfer. In response to the interim audit report, RRFC filed the necessary reports for 2002 that correctly disclosed these transfers

## **Finding 5. Disclosure of Occupation and Name of Employer**

### **Summary**

RRFC did not adequately disclose occupation and name of employer information for 200 contributions from individuals totaling \$132,811. No "best efforts" to obtain, maintain and submit this information was demonstrated by RRFC. In response to the interim audit report, RRFC materially complied by filing amended reports disclosing 69% of the missing contributor information.

### **Legal Standards**

**Required Information for Contributions from Individuals** For each itemized contribution from an individual, the committee must provide the following information:

- The contributor's full name and address (including zip code);
- The contributor's occupation and the name of his or her employer,
- The date of receipt (the date the committee received the contribution);
- The amount of the contribution, and
- The election-to-date (or election cycle-to-date in the case of authorized candidate committees) total of all contributions from the same individual. 2 U.S.C. §434(b)(3)(A) and 11 CFR §§100.12 and 104.3(a)(4).

**Best Efforts Ensures Compliance.** When the treasurer of a political committee shows that the committee used best efforts (see below) to obtain, maintain, and submit the information required by the Act, the committee's reports and records will be considered in compliance with the Act. 2 U.S.C. §432(h)(2)(i).

**Definition of Best Efforts.** The treasurer and the committee will be considered to have used "best efforts" if the committee satisfied all of the following criteria

- All written solicitations for contributions included
  - A clear request for the contributor's full name, mailing address, occupation, and name of employer, and
  - A statement that such reporting is required by Federal law.
- Within 30 days after the receipt of the contribution, the treasurer made at least one effort to obtain the missing information, in either a written request or a documented oral request.
- The treasurer reported any contributor information that, although not initially provided by the contributor, was obtained in a follow-up communication or was contained in the committee's records or in prior reports that the committee filed during the same two-year election cycle 11 CFR §104.7(b)

### **Facts and Analysis**

After reviewing all contributions from individuals in amounts aggregating over \$200, the Audit staff identified 200 contributions totaling \$132,811 (42% of contributions from individuals) from 159 contributors that did not have an occupation and/or name of employer reported properly. Of the 200 errors identified, 174 (87%) were either blank or "requested" was disclosed. The remaining errors (13%) consisted of incomplete disclosures (for example, an employer was disclosed but no occupation). In addition, the records provided to the Audit staff did not contain any solicitation material or follow-up requests for missing contributor information.

At the exit conference, the Audit staff presented this matter to RRFC representatives. No questions were posed or comments offered by the representatives. In response to the exit conference, RRFC representatives submitted documentation suggesting that they had complied with the "best efforts" requirements for obtaining occupation and name of employer information. RRFC stated that each written solicitation for a contribution included a clear request for the occupation and name of employer information. Also a follow-up request for the missing information was made if the information was not provided with the contribution. As additional support, representatives also provided a copy of one letter sent to a contributor lacking this information, who was not one of the individuals included as an error.

The response submitted by RRFC did not demonstrate "best efforts" were made to obtain, maintain and submit missing occupation and name of employer information. The response did not establish that

- Follow-up requests were sent to all contributors lacking the occupation and name of employer information, or,
- Responses were received from contributors and the contributor information was updated in the disclosure reports

**Interim Audit Report Recommendation and Committee Response**

The Audit staff recommended that RRFC take the following action.

- Provide documentation such as the initial solicitation devices, phone logs, returned contributor letters, completed contributor contact information sheets or other materials which demonstrated that best efforts were used to obtain, maintain, and submit the required disclosure information, or
- Absent such a demonstration, make an effort to contact those individuals for whom required information is missing or incomplete, provide documentation of such contacts (such as copies of letters to the contributors and/or phone logs), and file complete amended reports to disclose any information obtained from those contacts.

In response to the interim audit report, RRFC filed an amended report with updated contributor information for most of the omissions noted above. In addition, RRFC submitted a sample of letters sent to contributors to obtain the missing information.

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Rick Renzi for Congress (AUG-13)  
Audit Staff Analysis of Loans Based on Response to the IAR

Count	Source of Funds	Date Funds Transferred to Candidate	Date Funds Loaned to RRFC	Loan Amount	RRFC Position on Source of Funds for Loan	Audit Staff Position on Source of Funds for Loan	Permissible Loan per Audit Staff	Impermissible Loan per Audit Staff
1	Renzi & Co., Inc	12-10-01	12-11-2001	\$6,090	Repayment to Candidate	Candidate is borrowing additional amounts. Therefore, the source is Renzi & Co. and loan impermissible.		\$6,090
2	Renzi & Co., Inc.	12-10-01 12-11-01	12-18-2001	\$31,000	Loan Repayment to Candidate	Candidate is borrowing additional amounts. Therefore, the source is Renzi & Co. and loan impermissible.		\$31,000
3	Renzi & Co., Inc.	12-20-01	12-20-2001	\$50,000	Loan Repayment to Candidate	Candidate is borrowing additional amounts. Therefore, the source is Renzi & Co. and loan impermissible.		\$50,000
4	Renzi & Co., Inc.	12-28-01	12-28-2001	\$35,000	Loan Repayment to Candidate	Candidate is borrowing additional amounts. Therefore, the source is Renzi & Co. and loan impermissible. Elgin Property Funds flow through Renzi & Co; funds appear to be permissible.	\$35,000	
5	Renzi & Co., Inc	12-28-01	12-28-2001	\$272,000	Loan Repayment to Candidate			\$272,000
6	Renzi & Co., Inc.	3-28-02	3-28-2002	\$70,000	Distribution to Candidate	The source is Renzi & Co and therefore, the funds impermissible it appears permissible	\$70,000	
7	Fountain Realty & Development	12-18-01	12-19-2001	\$10,000	Distribution to Candidate	Source is Fountain, therefore, funds are impermissible.		\$10,000
8	Fountain Realty & Development	3-14-02	3-28-2002	\$35,000	Loan Repayment to Candidate	RRFC repaid Candidate \$70,000; who in turn loaned funds to Fountain. This is a repayment of those funds and excluded as duplicative.	\$35,000	
9	Fountain Realty & Development	3-14-02	3-28-2002	\$25,000	Loan Repayment to Candidate	RRFC repaid Candidate \$70,000; who in turn loaned funds to Fountain. This is a repayment of those funds and excluded as duplicative	\$25,000	
10	Fountain Realty & Development	6-28-02	6-28-2002	\$51,000	Loan Repayment to Candidate	Although no detailed documentation on original loan;	\$51,000	
It is likely funds are permissible							\$216,000	\$369,090
Total				\$ 585,090				

# Rick Renzi for Congress (A03-13) Audit Staff Flowchart of Funds Relative to Candidate Loans

ATTACHMENT 2 (one page)

Created By: A. Boniewicz

